UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

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SR INTERNATIONAL BUSINESS INSURANCE CO. LTD.,

Plaintiff-Counterclaim Defendant,

-v.-

WORLD TRADE CENTER PROPERTIES LLC, et al.

Defendants-Counterclaimants.

01 Civ. 9291 (JSM)

**OPINION & ORDER**

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ALLIANZ INSURANCE COMPANY, et al.

Plaintiff-Counterclaim Defendants,

-v.-

WORLD TRADE CENTER PROPERTIES LLC, et al.,

Defendant-Counterclaimants.

02 Civ. 0017 (JSM)

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JOHN S. MARTIN, Jr., District Judge:

This litigation has already given rise to several opinions of the Court. Familiarity with those opinions and the background of this litigation is assumed.

While there are substantial disputes concerning the terms of the insurance coverage for the World Trade Center, the parties are in agreement that all of the policy forms under discussion as of September 11, 2002, contained a provision that any dispute

concerning the amount of the loss was to be resolved by an appraisal process pursuant to which each side would select a disinterested appraiser and, if the two appraisers could not agree on the amount of the loss, the dispute would be resolved by an umpire selected by the appraisers.[1]

Pursuant to N.Y. C.P.L.R. 7601, Allianz now seeks to compel the Silverstein Parties to submit their dispute concerning the amount of the loss to the appraisal process. While some of the other insurers have stated that they too might decide to seek an appraisal, other insurers have declined to invoke the appraisal mechanism, preferring to have the amount of the loss determined by a jury. While the Silverstein Parties could assert appraisal rights against all of the insurers, they have declined to do so because they believe that the appraisal provision has been

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[1]For example, the Allianz Policy provides that:

> In the case the Insured and this Company shall fail to agree as to the amount of the loss or damage to the property insured, each shall, on the written demand of either, select a competent and disinterested appraiser. The appraisers shall select a competent and disinterested umpire. If failing for fifteen (15) days to agree upon such umpire, then on request of the Insured or the Company, such umpire shall be selected by a judge or a court of record in the state in which the insured property is located.
> Each appraiser shall then appraise the loss and damage, stating separately actual cash value at time of loss and amount of loss. If failing to agree the appraisers shall submit their differences to the umpire. An agreement of the amount of loss in writing of any two (2) shall determine the amount of loss.

(Massopust Aff. Ex. C at p. EPIF 6.)

preempted by the Air Transportation and System Stabilization Act ("the Act"), Pub. L. No. 107-42, 115 Stat. 230 (Sept. 22, 2001) (amended by the Aviation and Transportation Security Act, Pub. L. No. 107-71, 115 Stat. 597 (Nov. 19, 2001) ("Aviation Security Act")), in which Congress granted to this Court "original and exclusive jurisdiction over all actions brought for any claim . . . resulting from or related to the terrorist-related aircraft crashes of September 11, 2001." The Act § 408(b). The Silverstein Parties also argue that Allianz's application is both premature and too late and that the Court should exercise its discretion to deny Allianz its appraisal rights because it would subject them to possibly inconsistent results from the jury trial as to some insurers and the appraisal proceedings as to others.

The Silverstein Parties claim that Allianz's attempt to invoke its appraisal right is both premature and too late is without merit. There is nothing in the language of the appraisal provision that suggests that an insurer must hire experts to evaluate the loss and then engage in good faith negotiations with the insured over the amount of the loss before it may invoke the appraisal process. Indeed, the appraisal provision itself suggests that it is the appraisers appointed by the parties who are to engage in the good faith effort to resolve the dispute before it is submitted to an umpire. See supra note 1. It makes no sense to suggest that the parties must bear the expense of

hiring experts to evaluate a loss before they retain the services of "an impartial appraiser."

The Silverstein Parties' contention that Allianz has waited too long to enforce its rights is based on the argument that one can waive rights to arbitration or appraisal by participating in litigation without asserting those rights. See Sherill v. Grayco Builders, Inc., 64 N.Y.2d 261, 273-74 (1985). Here, however, Allianz reserved its right to demand appraisal in its Reply to the Silverstein Parties' Counterclaim, and spent a substantial portion of the time between the filing of that pleading and the filing of its present motion attempting to negotiate an agreement for an appraisal process with the various insurers and the insured. Thus, by its conduct, Allianz did not waive its appraisal rights.

There is also no merit to the argument of the Silverstein Parties that the enforcement of Allianz' appraisal rights would be inconsistent with Congress' grant to this Court of exclusive jurisdiction over actions "resulting from of related to" the terrorist attacks on September 11th.

At the outset it should be noted that to construe the grant of jurisdiction to deny Allianz a contractual right that it has under New York law would raise serious constitutional issues. Under Article III of the Constitution, the federal courts' jurisdiction is limited to cases "arising under this

Constitution, the Laws of the United States," and certain other specifically designated types of cases. U.S. Const. art. III, § 2, cl. 1. See Insurance Corp. of Ireland, Ltd. v. Compagnie des Bauxites de Guinee, 456 U.S. 694, 701, 102 S.Ct. 2099, 2103 (1982)("Federal courts are courts of limited jurisdiction."). Congress lacks the power to confer jurisdiction on the federal courts over purely state claims such as these. See Verlinden B.V. v. Central Bank of Nigeria, 461 U.S. 480, 491, 103 S.Ct. 1962, 1970 (1983) (". . . Congress may not expand the jurisdiction of the federal courts beyond the bounds established by the Constitution.").

The Silverstein Parties do not argue that Congress based its grant of jurisdiction to this Court on its powers under the Commerce Clause, and there is no support for such a claim in the legislative history. Rather, they argue that the grant of jurisdiction can be sustained in this case because there is at least constitutional diversity of citizenship here.[2] However, even if this were so, when the only basis of jurisdiction is diversity of citizenship, federal courts must apply state law. Erie R. Co. v. Tompkins, 304 U.S. 64, 78, 58 S.Ct. 817, 822 (1938). As Justice Brandeis observed in Erie:

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[2] While the Constitution permits the judicial power to extend to cases "between citizens of different states", Congress has restricted federal court jurisdiction to those cases in which there is complete diversity between all plaintiffs and all defendants. See Owen Equipment & Erection Co. v. Kroger, 437 U.S. 365, 373, 98 S.Ct. 2396, 2402 (1978).

> Congress has no power to declare substantive rules of common law applicable in a state whether they be local in their nature or 'general,' be they commercial law or a part of the law of torts. And no clause in the Constitution purports to confer such a power upon the federal courts.

304 U.S. 64, 78, 58 S.Ct. 817, 822.

Thus, in a diversity case, the contractual right to submit a factual dispute to an appraiser, if such a right is enforceable under state law, is one that the federal courts are required to enforce under Erie. Cedant Corp. v. Forbes, 70 F. Supp. 2d 339,344-45 (S.D.N.Y. 1999).

Given the well established canon of statutory construction that statutes should be construed to avoid constitutional questions, Seminole Tribe of Florida v. Florida, 517 U.S. 44, 182, 116 S.Ct. 1114, 1184 (1996); Edward J. DeBartolo Corp. v. Florida Gulf Coast Building & Constr. Trades Council, 485 U.S. 568, 575, 108 S.Ct. 1392, 1397 (1988), the Court would be inclined to construe the Act's grant of jurisdiction as not extending to these claims between the insurers and their insureds. But even if there were no constitutional issue presented, there is no basis for finding that when Congress conferred jurisdiction on this Court for all actions relating to the events of September 11th, it meant to deprive parties of their contractual right to appraisal or arbitration. Indeed, there is a serious question whether the grant of jurisdiction in the Act applies to this case.

The background and legislative history of the Act have been fully set forth in the thorough opinions of my colleagues, Judge Cote and Judge Pauley, in their thoughtful opinions in International Fine Art and Antique Dealers Show Ltd. v. ASU Intern., Inc., 2002 WL 1349733 (S.D.N.Y. Jun 20, 2002) (DLC) and Canada Life Assur. Co. v. Converium Ruckerversicherung (Deutschland) AG, 2002 WL 654124, (S.D.N.Y. Apr 19, 2002) (WHP), and need not be repeated here. Suffice it to say that the original purpose for that legislation was to limit the liability of the airlines whose planes were used in the terrorist attacks to the amount of their liability insurance and to provide an alternative method of compensating the victims of the attacks. Subsequently, the statute was amended to extend this same limitation on liability to persons with a property interest in the World Trade Center. Aviation Security Act § 201(b)(2) (amending the Act § 408(a)). There is nothing in the legislation or its history to suggest that Congress in any way intended to affect the rights and obligations between those having a property interest in the World Trade Center Complex and their insurers.

The opinions of Judges Pauley and Cote demonstrate that the legislative history and purpose of the Act do not support a reading of the jurisdictional grant that would extend the Act's coverage to all cases that relate to the events of September 11th. However, the Court need not decide whether Congress either

intended to or could vest this Court with exclusive jurisdiction over an action between the Silverstein Parties and their insurers, since there is no basis to find that, in conferring jurisdiction of this Court, Congress intended to strip either the insurers or the insureds of their right to have the amount of the loss determined in an appraisal proceeding. There is nothing in either the legislative history of the Act or in the cases cited by the Silverstein Parties that requires such a result.

While the November, 2001, amendment to the Act extended its liability protections to those "with a property interest in the World Trade Center," the Act did not in any respect attempt to alter the substantive rights existing among those property owners and their property casualty insurers, nor is there any reference to that relationship in the legislative history. The legislative history indicates that Congress conditioned the protection it provided to the property owners on the satisfaction of "all contractual obligations to rebuild or assist in the rebuilding of the World Trade Center." H.R. Conf. Rep. 107-296 at 81 (Nov. 16, 2001), reprinted in 2001 U.S.C.C.A.N. 589, 619. However, this provides no basis for finding that Congress was attempting to alter the substantive rights existing among the property owners and their insurers. To the contrary, such a statement by Congress suggests that they were leaving those rights and obligations as they were under existing law.

None of the cases cited by the Silverstein Parties requires a finding that the grant to this Court of exclusive jurisdiction over these actions removes from the Court its discretion to refer the valuation issue to the appraisers. While the cases cited by the Silverstein Parties do involve situations in which the courts have found that a Congressional grant of exclusive jurisdiction to a particular court may be inconsistent with the recognition of a party's right to compel arbitration, those cases involve statutory schemes involving a strong federal interest where it was reasonable to assume that Congress wanted all legal issues decided by a particular court.

For example, in Kaiser Aluminum & Chemical Corp. v. Bonneville Power Administration, 261 F.3d 843 (9th Cir. 2001), the defendant was a federal agency established by Congress to market hydroelectric power generated by dams along the Columbia River. In rejecting Kaiser's demand for arbitration, the Court reasoned:

> [I]n CP National Corp. v. Jura, 876 F.2d 745, 747-48 (9th Cir.1989), we held, regardless of whether petitioners characterize their claims as contract actions, Congress has given us "exclusive jurisdiction over what is in reality a challenge to a final action of BPA taken pursuant to statutory authority." We reasoned that "jurisdiction under the Act should be a function of the agency whose actions are being challenged rather than a function of the cause of action which petitioner asserts." Id. at 747 (citation and internal quotation omitted).
>
> Kaiser admits that it is primarily challenging action taken by the BPA pursuant to the Preference Act and the Northwest Power Act. Because Kaiser is challenging BPA action taken under those Acts, Congress has expressly bestowed exclusive jurisdiction to resolve the matter on us. We cannot relinquish that jurisdiction to an arbiter despite

> Kaiser's characterization of its claim as one for breach of contract.

261 F.3d at 852.

While the federal interest in having the actions of a federal agency reviewed in a specifically designated federal court may be sufficient to override a party's contractual right to arbitration, there is no similar federal interest here that might justify depriving the insurers of their rights under the substantive law that applies in this case.

In Consolidated Rail Corp. v. Illinois, 423 F. Supp. 941 (1977), also relied upon by the Silverstein Parties, a special three judge court established under the Regional Rail Reorganization Act of 1973, §§ 209(e)(1)(C), as amended 45 U.S.C.A. §§ 719(e)(1)(C), considered the validity of an injunction obtained by the State of Illinois in the Eastern District of Illinois which prohibited Conrail from implementing a route change adopted by the United States Railway Association under the Final System Plan. The injunction was granted on the basis of a finding that Conrail had violated § 206(d)(4) of The Regional Rail Reorganization Act of 1973. That Act provided:

> Notwithstanding any other provision of law, any civil action . . . challenging the legality of any action of the Association, or any failure of the Association to take any action, pursuant to authority conferred or purportedly conferred under this Act . . . shall be within the original and exclusive jurisdiction of the special court.

The three judge court vacated the injunction, holding:

> We conclude that USRA's actions were sufficiently connected to the proceedings in the Illinois district court to satisfy the requirements of § 209(e)(1)(C).

423 F.Supp. at 947.

Rather than supporting the position of the Silverstein Parties that a grant of exclusive jurisdiction should be broadly construed, the opinion in Consolidated Rail Corp. supports the opposite conclusion, for just after the above quoted language the court observed:

> We note that any possible apprehension based on our determination today that the Special Court will be inundated with contract claims that bear a relation to the Act is misconceived. The major fact in the present case that allows for exclusive jurisdiction is the conditional designation of the Paris-Lawrenceville segment of the Cairo line in the FSP. It is USRA's failure to certify this portion of the Cairo line for conveyance that provides its connection to this action. Absent the alternative designation, there would be little basis for finding that the district court action was a challenge to the actions of the USRA.

423 F. Supp. at 947.

Nor do the decisions cited by the Silverstein Parties that dealing with the power of the Bankruptcy Court to stay arbitration relating to core proceedings support the conclusion that the jurisdictional grant at issue here precludes recognition of the insurers' appraisal rights. See In re Crysen/Montenay Energy Co., 226 F.3d 160 (2d Cir. 2000); In re United States Lines, Inc., 197 F.3d 631 (2d Cir. 1999). As the Court explained in In re Crysen/Montenay Energy Co.:

> The issue in U.S. Lines was whether a bankruptcy court *may decline* to stay a *core* proceeding in favor of arbitration. As we noted there, the presumption in favor of arbitration generally will trump the lesser interest of bankruptcy courts in adjudicating non-core proceedings that could otherwise be arbitrated. We also

> explained that "even" in core proceedings, in which the interest of the bankruptcy court is greater, the bankruptcy court nonetheless *might* lack discretion to decline to stay in favor of arbitration. The unmistakable implication is that bankruptcy courts generally *do not* have discretion to *decline* to stay *non-core* proceedings in favor of arbitration, and they certainly have authority to grant such a stay.

226 F.3d at 166 (Emphasis added; italics in original).

In sum, the court finds nothing in either the Act, its legislative history, or the cases cited by the Silverstein Parties that would strip the Court of its discretion to enforce the appraisal provision in question. However, the issue remains as to how the Court should exercise that discretion in this case.

The Silverstein Parties argue that the Court should refuse to exercise its discretion to order an appraisal proceeding because a finding by the Court that the appraisal proceeding is not preempted by the Act may be reversed on appeal and, therefore, the issue would have to be tried a second time. However, any ruling of a District Judge may be reversed on appeal and an erroneous ruling on a single issue will often result in the retrial of complex issues. Moreover, even if it would be appropriate for the Court to exercise its discretion to decline to compel an appraisal if it was convinced that there was a serious possibility that its ruling would be reversed on appeal, this is not such situation. While this may be a case of "often in error but never in doubt," the Court is persuaded that there is very little likelihood that the Second Circuit would find that

the Act precluded this Court from recognizing the insurers' appraisal rights.

Nor is the Court persuaded that the possibility of differing results in parallel proceedings militates against the right of Allianz to have the damage issue resolved in accordance with the terms of its contract with the Silverstein Parties. In entering into separate contracts with different insurers, the Silverstein Parties took the risk that there would be differences in the amounts they recovered from various insurers. Indeed, while the Silverstein Parties are attempting to recover twice the face value of their policies from the insurers against whom they have asserted claims in this litigation, they have already settled against other insurers for the face amount of those policies because they recognized that the language of those policies is different from that in the policy forms they contend govern their relations with insurers.

There is, however, one consideration that may militate against the full enforcement of the appraisal provision agreed to by the parties. The enforcement of appraisal rights in this case, where only some of the insurers are seeking an appraisal, may unfairly multiply the proceedings in which the Silverstein Parties are forced to litigate the valuation issue. See Penn Central Corp. v. Consolidated Rail Corp., 56 N.Y.2d 120, 130 (1982). One possible remedy is for the Court to substitute itself for the neutral umpire to whom the dispute is to be

submitted if the appraisers can not agree. Clark v. Kraftco Corp., 17 F. Supp. 2d 358, 361 (S.D.N.Y. 1998). While this resolution of the issue appears to be the most appropriate at the moment, this case has not yet progressed to the point at which a final decision should be made with respect to this question. Several of the insurers are in the process of submitting summary judgment motions and it is not yet clear whether all of the insurers will be joined in a single trial.

Therefore, it seems appropriate at this time to enforce the appraisal provision to the extent of requiring the parties to designate their appraisers and to have the appraisers attempt to reach agreement on the amount of the loss, while holding in abeyance a final decision as to whether, in the event that the appraisers cannot agree, they should choose an umpire or the Court should substitute itself for the umpire.

**SO ORDERED.**

Dated: New York, New York

August, 2002

JOHN S. MARTIN, JR., U.S.D.J.

Copies to:

For Plaintiff-Counterclaim Defendants:

John B. Massopust
Zelle, Hofmann, Voelbel, Mason & Gette LLP
33 South Sixth Street
City Center -Suite 4400
Minneapolis, Minnesota 55402

For Defendant-Counterclaimants:

Herbert M. Wachtell
Wachtell, Lipton, Rosen & Katz
51 West 52nd Street
New York, NY 10019-6150